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SUBJECT: "UNTIED FOOD AID" - WFP STUDY FOR UNCTAD

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Summary

1. (SBU) The WFP Secretariat has shared with the US Mission a paper prepared for the United Nations Conference on Trade and Development (UNCTAD) entitled: "Food Aid and the Untying of Aid: Opportunities and Challenges for the Least Developed Countries." The key premise for the untying of food aid (i.e., provision of cash to buy food anywhere) is that developing countries, including the Least Developed Countries (LDCs), will be able to compete fairly on the global market for procurement tenders to provide food aid. Although untied food aid has been gradually increasing, of the 10.2 million tons of food aid delivered globally (all spigots) in 2003, 7.6 million tons (75 percent) was procured in the donor countries. WFP has had favorable experiences in local purchases in Burkina Faso, Cambodia, Ethiopia, Malawi, Mozambique, Nepal, Sudan, Tanzania, Uganda and Zambia - where, in recent years, WFP has procured on average about U.S. dollars (USD) \$50 million worth of food. However, the potential for an LDC to take advantage of procurement opportunities forthcoming from the untying of food aid would heavily depend on an enabling environment for well-functioning competitive markets being established and increased investment in rural areas, particularly transport and storage infrastructure. WFP's report concludes that "until the results of these investments and the enabling environment take hold, untying food aid is likely to further marginalize the poorest countries as they may lose a vital resource in reducing risk, vulnerability and hunger, while gaining little in trade." In US Mission's view, this study rightly shows that local food aid procurement, particularly in LDCs, is certainly "no silver bullet" to meeting the food aid needs of the world's hungry poor. End summary.

Background

2. (U) The agreement in 2001 by members of the OECD's Development Assistance Committee to untie seven types of Official Development Assistance given to the Least Developed Countries (LDCs) was a landmark decision and a significant step towards improving the effectiveness of aid. The possibility of untying other types of aid, including food aid, continues to be debated within the OECD and in a variety of other arena - in particular, the World Trade Organization. The concern over food aid centers on the difficulty some donors would have in providing untied food aid. Donors are debating whether the efficiency gains of untying food aid compensate for the likely reduction in a resource that provides considerable benefit in directly reducing the hunger of marginalized or crisis-affected populations often by-passed by other types of assistance. This debate is particularly relevant to most LDCs, who would have difficulty competing for increased trade opportunities,

and would be the most hurt by reductions in food aid resources.

3. (U) The World Food Program (WFP) provides over a third of

global food aid and has consistently been the largest food aid procurer in developing countries, accounting for 75 percent of the food aid purchased in recent years. Although untied food aid is increasing, WFP still receives over half its food resources through tied "in-kind" donations.

14. (SBU) The key premise for the untying of food aid is that developing countries, including the LDCs, will be able to fairly compete on the global market for procurement tenders to provide food aid.

The "long, uphill-all-the-way-to-the-very-end road" for the LDCs according to WFP

15. (SBU) WFP's report cites the following:

- The reality of WFP's experience of working in LDCs, highlights the concern that most LDCs would actually lose from the untying of food aid. At present, poverty, inadequate infrastructure, lack of investment in agriculture, limited export-earning capacity and weak institutions will limit the ability of many LDCs to significantly expand export sales to capture trade benefits from the untying of food aid. At the same time, the process of getting to a well-functioning, liberalized market is expected to be a long and difficult path of adjustment, particularly for the poorest, net food-importing developing countries;
- A comparison of American and European Union food aid flows shows a clear decline in European Union food aid after the European Commission and European member countries moved to untie food aid;
- Purchasing from LDCs is often limited by the capacity of local traders to provide large amounts of cereals of an appropriate quality for food aid on demand. Given the political and economic context of these countries, private sector traders are often faced with uncertainty, security risk, poor infrastructure and poor institutions, creating disincentives for investment and inhibiting the expansion of well-functioning food markets;
- Over the past five years there has not been a significant increase in purchasing from LDCs, despite cash being available. Instead, purchases have increased in other developing countries - mainly large exporters of cereals like Turkey and South Africa - who are better placed in terms of location and capacity to respond to the large and sudden demands for food aid that are typical of emergency operations.

The upside and the downside of local purchases

16. (SBU) The upside of local food aid purchases. Through its extensive experience in food procurement in developing food markets, WFP has helped many traders meet the stringent

requirements of international procurement. WFP's food procurement is based on the principle of encouraging competitive practices among commercial traders while ensuring value for money in the purchase of food commodities. Based on lessons learned through various studies of WFP's food procurement, LDCs can benefit from the following opportunities if untied food aid were to increase:

- By imparting "international standard business practices," procurement activities can support medium-level traders, transfer skills, and facilitate business networks between traders in neighboring countries;
- Sustained procurement in a market will generate sufficient confidence for medium-sized traders to invest in securing supply lines to meet tenders;
- Triangular transactions facilitate international trade networks.

17. (SBU) The downside of local purchases. The difficulties WFP has found in undertaking procurement from LDCs with weakly developed food markets include the following:

- Standard business procedures discourage smaller traders or those who are not formally established from participating in tenders, limiting WFP's suppliers in LDCs;
- As food aid needs vary in levels and locations each year, WFP is not seen as a regular buyer on the market. Therefore only larger traders who have well-established stores and access to trade finance are willing to regularly supply WFP;
- Few traders are able to expand their supply of properly graded, quality food products where government investments have not been made in food grading and standards;
- WFP regularly encounters problems with trader reliability and quality. Thus a great deal of supervision of contracts is required to ensure timely food aid delivery, an administrative cost borne by WFP as part of its efforts to increase procurement in the poorest developing countries;
- Weak transport and trade infrastructure reduce the

competitiveness of traders and can reduce reliability of timely delivery of contracts.

The WFP report's conclusion

18. (SBU) The potential for an LDC to take advantage of procurement opportunities forthcoming from the untying of food aid depends clearly on an enabling environment for well-functioning competitive markets being established and increased investment in rural areas, particularly transport and storage infrastructure. Until the results of these investments and the enabling environment take hold, untying food aid is likely to further marginalize the poorest countries as they may lose a vital resource in reducing risk, vulnerability and hunger while gaining little in trade.

Comment from Ambassador Hall

19. (SBU) In this fiftieth anniversary year of U.S. Public Law 480, we are reminded that, since 1954, the USG has contributed more than USD \$50 billion to finance more than

367 million metric tons of U.S.-grown food to over 150 food insecure countries. Unwavering congressional support over five decades is due, in no small measure, to the blessings of our national agricultural abundance. As we look to the future, we will undoubtedly need to be creative in identifying additional mechanisms to supply food aid, given the exponential growth in complex and intractable emergencies. But let us keep very much in mind (as this WFP report rightly observes) that local procurement, particularly in LDCs, is certainly "no silver bullet" to meeting the food aid needs of the world's hungry poor.

110. Minimize considered for Baghdad.
Hall

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